No. 2628

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

In the Matter of R. S. MILLER,
A Bankrupt.

OLMSTED-STEVENSON COMPANY
(a corporation),
Petitioner,

vs.

R. S. MILLER,
Respondent.

BRIEF FOR PETITIONER.

JOHN B. CLAYBERG,
Attorney for Petitioner.

Filed this.....day of October, 1915.

FRANK D. MONCKTON, Clerk.

By.....Deputy Clerk.

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This hearing is upon a petition to revise and review an order of the District Court of the United States for the District of Montana, made and entered in the above matter on or about the 27th day of March, 1915.

Statement of Facts.

The undisputed facts, as disclosed by the record, are that the bankrupt, R. S. Miller, had entered a

piece of government land as a homestead under the Acts of Congress, in September, 1910 (Tr. p. 14), and was in possession thereof as such homesteader during the years 1913 and 1914; that in the fall of 1913 he planted fifty acres of this homestead in winter wheat, which at the time of the filing of his petition in bankruptcy was a growing crop (Tr. p. 14); that on February 5, 1914, he filed his voluntary petition to be adjudged a bankrupt, and that he was adjudged a bankrupt and received a discharge in April, 1914. The petitioner was named in the bankrupt's schedule of creditors for the amount claimed as due it. It proved its claim, which was recognized and allowed by the trustees.

It seems that the bankrupt did not place in his schedule of assets and property such growing crop of grain, and, after his discharge but prior to the closing of the estate, petitioner herein sought to have the bankruptcy proceeding opened and the bankrupt directed and ordered to amend his schedule of property and assets so that it might include the growing crop of wheat (Tr. pp. 3 *et seq.*).

The bankrupt contested the relief asked on the ground that the crop was exempt to him under the statutes of Montana, and also under the laws of the United States, and insisted that the trustee in bankruptcy and the petitioner were guilty of such laches as to be estopped from being entitled to the relief asked (Tr. pp. 10 *et seq.*).

The Referee who heard the matter upon the original petition, found in favor of your petitioner (Tr.

p. 20), but upon the petition of the bankrupt to the District Court of the United States for the District of Montana, that court reversed the decision of the Referee (Tr. pp. 29 and 84).

Argument.

But two questions seem necessary to be considered by this court upon this hearing, namely: (I) Was the growing crop of wheat an asset of the bankrupt which passed to the trustee for the benefit of creditors; and (II) Is petitioner estopped from procuring the relief sought because of laches in the filing of his petition?

Logically, these questions should be considered in their inverse order, because if the petitioner is estopped by laches, the first question becomes immaterial.

I.

WAS THE PETITIONER ESTOPPED BY LACHES?

It is too well settled a proposition to require the citation of authority, that a bankrupt court sits as a court of equity and is governed by equitable rules. The question of laches must, therefore, be determined by the application of equitable rules as established in the federal courts of the United States. It is held in the case of *Valvona, etc. v. Marchiony,* 207 Fed. 380, that laches in equity is based upon the doctrine of an equitable estoppel against the party

bringing the suit or proceeding. It is held in *Galliher v. Cadwill,* 145 U. S. 368, that in applying the doctrine of laches or estoppel, courts of equity proceed upon the assumption that the party to whom laches is imputed has had full knowledge of his rights and an ample opportunity of establishing them; that by reason of his delay the adverse party has good reason to believe that the alleged rights are deemed worthless, or have been abandoned, and because of the change in conditions or relations during the period of delay it would be unjust to the defendant to permit the opposing party to assert his rights. Therefore, unless the bankrupt has disclosed some injury or prejudice occurring to him or his estate during the delay of petitioner in filing its original petition, or that he has changed his position relying upon the non-action of this petitioner, so that the granting of the order prayed for would be inequitable, the question of laches amounts to nothing.

Nowhere in any of the pleadings or proceedings is it alleged that the bankrupt had changed his position or was injured by relying on the fact that the petitioner had waived or abandoned its claim.

We concede that upon this hearing this court may not consider disputed questions of fact, only questions of law can be considered. Whether the evidence introduced is sufficient to sustain the order sought to be reviewed is a question of law and may therefore be considered by this court.

Kirsner v. Taliaferro, 202 Fed. 51;
In re Frank, 182 Fed. 794;

In re Lee, 182 Fed. 579;
In re Knosher, 197 Fed. 136 (this court).

True, it is alleged in the bankrupt's answer to the original petition filed herein, that the petitioner,

> "with full knowledge of all the facts in this case as aforesaid, consented, advised, and knowingly permitted the said trustee to proceed with the administration of said estate and set aside to this bankrupt his exemptions including the real estate on which said crop was growing, and to permit this bankrupt in good faith to expend his labor, time, material and money in taking care of, harvesting and marketing said crop, and that by reason thereof said petitioning creditor now is estopped from claiming or requiring this bankrupt to surrender said crop or to surrender the proceeds of said crop in order that the same may be administered and distributed to this bankrupt's creditors herein" (Tr. p. 17).

But there was no allegation that he took care of, harvested and marketed the crop in reliance upon the silence of this petitioner, or that he was led to spend his money or change his position relative to the crop in reliance upon any action of your petitioner. There was not one syllable of evidence offered at the hearing before the Referee to support the above allegation. All the evidence introduced in behalf of the bankrupt simply tended to show that he acted in good faith and upon the advice of his attorneys in not placing this growing crop in his schedule of assets and property (Tr. pp. 53-54, 56, 71); that petitioner's agent knew of the existence of the crop; knew that the bankrupt claimed

that it was exempt and that the land upon which the crop was growing had been set aside to him as exempt property. There was absolutely no evidence introduced even tending to show that your petitioner ever consented to anything or that the bankrupt spent his time and money in caring for, harvesting and marketing the crop in reliance on the inaction of your petitioner to his injury, but the testimony introduced conclusively shows that he performed all these acts because he believed and had been advised that he was *the owner of the crop* (Tr. pp. 53, 54, 56, 71). There was no testimony to indicate that your petitioner had led the bankrupt to believe, or that the bankrupt did believe, that your petitioner had waived any rights which it might have had or claimed, or would never attempt to enforce them. There is nothing to bring the matter within the doctrine of *Galliher v. Cadwill, supra.* The bankrupt doubtless believed that he was the owner of the crop and that no one questioned it.

It appears exceedingly strange to us that if the bankrupt had relied upon the acquiescence and silence of your petitioner concerning the ownership and right to the crop, he should have kept so accurate an account of the time, money and labor he placed upon the growing crop, even to the value of harrowing the same (Tr. pp. 72 to 82). Presumably he made his memoranda of expenses at the time he incurred the same (Tr. p. 72), realizing that it was doubtful as to his ownership of the crop, and intended to "play safe", so that he might recover his

expenses of caring for the crop in case the matter should finally be decided against him.

Under the circumstances disclosed by the pleadings and testimony we concede that it would be only equitable and right that the bankrupt be allowed to retain out of the proceeds of this crop every dollar he has spent in caring for, harvesting and marketing the same, and reasonable compensation for any time or labor he expended, together with a reasonable rental for the land upon which this crop was growing. We have no doubt that he acted in good faith and upon the advice of his attorneys, although he evidently was aware of the fact that his rights were doubtful. We cannot consent, however, that he be allowed to retain anything beyond what would be sufficient to make him whole. This would be inequitable to the creditors and place a premium upon dishonesty of a debtor.

It seems that the bankrupt insisted in the court below that the trustee was agent for the creditors and that he, the trustee, was guilty of such laches as to prevent him from claiming this crop as a part of the estate of the bankrupt for distribution among his creditors, and that petitioner, being one of the creditors, was and is bound and concluded thereby. It appears from the opinion of the court below that he coincided with this view and held the trustee guilty of such laches as to bar petitioner.

In this view, we insist that both were mistaken. The court says:

> "No fraud appearing, it is final and concludes creditor. The bankrupt assumed all risk and hazard of failure, the trustee none, and in justice to the former he is entitled to whatever success was achieved" (Tr. p. 32).

The court disregarded the fact that the trustee had made no effort to have the bankrupt turn over this crop or its proceeds for the benefit of the creditors. He has always maintained the position that this crop was exempt. He states in his testimony that he was so advised by the bankrupt's attorneys.

The court was also evidently impressed with the idea that the laches of the trustee bound the creditors, and concluded that the trustee was estopped, and that therefore the creditors were also estopped. This idea was probably based upon the language of the court in the case of *In re Hansen,* 107 Fed. 252, cited in the brief for the bankrupt. This conclusion could only arise from the application of the principle that the trustee is agent for the creditors and that knowledge of an agent is always knowledge of the principal. The court in the case last cited, and the court below herein, failed to recognize the principle often announced by the federal courts that under the Bankrupt Act of 1898, the trustee does not stand in the relation of an agent of the creditors. The relationship between the trustee in bankruptcy and the creditor under the Act of 1898 is that of trustee and *cestuis qui trustent.* This from its very nature precludes the relationship of principal and agent. The trustee is at least a *quasi* officer of the

court, and is not bound by the actions, orders or directions of the creditors. This of itself precludes the relationship of principal and agent.

Under the Bankruptcy Act of 1867, a trustee was properly held to be the agent of the creditors, because they had full control, not only over the proceedings in bankruptcy but also over the trustee himself. There is no provision corresponding to this in the Act of 1898, and such relationship does not exist.

In re Columbia Iron Works, 142 Fed. 237;
In re Allen, etc., Co., 133 Fed. 388.

Inasmuch as under the Act of 1898 the trustee in bankruptcy is beyond the control of the creditors and is a *quasi* officer of the court, it would indeed be a strange doctrine to hold the creditors liable for his acts or knowledge. The trustee is charged with the duty of correcting the schedules of a bankrupt, the creditors have nothing to do with it. Suppose the trustee knowingly permits a large amount of the bankrupt's property to be omitted from the schedule of assets. Suppose no creditor has knowledge of the existence of such omission. To hold that the creditors should lose their claims upon such assets would so clearly be inequitable that it cannot stand as the law.

We therefore confidently submit that your petitioner was not guilty of such laches as would preclude it from receiving the relief sought by its petition.

II.

WAS THE GROWING CROP OF WHEAT AN ASSET OF THE BANKRUPT WHICH PASSED TO THE TRUSTEE FOR THE BENEFIT OF CREDITORS?

In order to properly determine this question a careful examination of the Bankrupt Act seems necessary.

Under Section 70, Subdivision A, the trustee is vested by operation of law with the title of the bankrupt to all

> "property which, prior to the filing of the petition, he could by any means have transferred, or which might have been levied upon and sold under judicial process against him." (Excepting, of course, property exempt under the Bankrupt Act.)

It has been held that by virtue of the above quoted language, an adjudication in bankruptcy brings all the property of the bankrupt, wherever situated, *in custodia legis,* and the court acquires full right and jurisdiction to administer the estate.

Knauth et al. v. Latham Co., 219 Fed. 71;
Lazarus v. Prentice, 234 U. S. 266.

It will be noticed that the language of Section 70, Subdivision A, above quoted, is in the alternative, and if the bankrupt is possessed of any property *"which he could by any means have transferred",* it passes to the trustee, as well as all of the property which "might have been levied upon and sold under judicial process against him".

In re Burnett Co., 29 Am. Bnk. Reg., 872.

In this case the bankrupt claimed as exempt an undivided one-half interest in a growing wheat crop.

The trustee declined to set it aside, and the Referee entered an order sustaining him. The bankrupt based his claim on a statute of Tennessee which prohibited a levy upon a growing crop until November 15th of each year, being after the maturity of the crops. The statutes of exemptions of that State did not include growing crops among exempt property. The State court had recognized the right to sell or mortgage growing crops. The federal court said:

> "It therefore follows that, not being exempt property and property which the bankrupt could have transferred at the time the petition was filed and the adjudication in bankruptcy made, title thereto must be held to have passed to the bankrupt, under provisions of Section 70 of the Bankrupt Act."

The Supreme Court of Montana has always recognized the right of the owner to mortgage growing crops.

Ford v. Sutherlin, 2nd Mont. 440;
Brande v. Babcock, 35th Mont. 256.

The same right is recognized by the statute of Montana.

Revised Code, Secs. 5773, 6824 and 6826.

Growing crops are not mentioned in the statute of exemptions of the State of Montana.

The court below held that crops growing on land included in a homestead entry were not property of the character which could vest in a trustee in bankruptcy. It is beyond our comprehension to understand why not. A crop growing on a home-

stead entry is not endowed with any peculiar sanctity, because of that circumstance, nor does any peculiarity of title or right attach to it. The homesteader is entitled to the possession of the land and all the fruits thereof so long as he complies with the provisions of the homestead law. He may raise any crop he desires and such crop is his own property. From the time the seed is placed in the ground, such ownership exists, and it continues during the germination of the seed and throughout its growth and ripening. It is always his own, and clearly comes within the common law designation of *fructus industriales.* He may sell, mortgage or do what he pleases with it. It may be seized, levied upon and sold by his creditors at any time. This has always been the rule of the common law.

Evans v. Roberts, 5 Barn. & Cress, 829;
Swafford v. Spratt, 67 N. W. 701;
Phillips v. Keysand, 56 Pac. 695;
Johnson v. Walker, 37 N. W. 640;
Polley v. Johnson, 35 Pac. 8;
Ayers v. Hawk, 11 Atl. 744.

It is impossible for us to understand why any difference should exist between the land held under a homestead entry and the land held under a contract of purchase from an individual owner. Unless the contract is complied with in the latter case, the person loses possession of the land, while in the former case he loses possession by failure to comply with the homestead law. The legal effect of noncompliance is the same in each case.

We cannot agree with the court below in its construction of Section 70 of the Bankrupt Act, wherein it limits the operation of its provisions to "property capable of change of ownership or enjoyment without recourse to or draft upon property and labor of the bankrupt". Section 70 provides that *all* property of the bankrupt which he could by any means have transferred or which might have been levied upon or sold under judicial process should pass to the trustee for the benefit of creditors. That the bankrupt could have sold and transferred this crop is, we submit, beyond question, and if he could have sold the same it might be levied upon by his creditors. The effectuality of a sale or of a levy is not the standard for the determination of *the right to sell or to make a levy.* Such right is determined by the ownership of the property. If the right of sale or levy exists, then the property passes to the trustee, irrespective of the question of what may be realized therefrom.

We are also of the opinion that the court erred in holding that

> "when the bankruptcy petition was filed, this crop had no separate existence. It was in the nature of an incident that followed the land. Its value was potential only—that might be created by the land and future labor. Of itself it had no transfer value".

We can conceive of no legal distinction between the law applied to this case and other cases of growing crops. There can be no doubt but that the bankrupt might sell growing crops to anyone.

If so, such crops were capable of separation from the land and would have a separate existence. Whether it could be levied upon is immaterial under Section 70, but in our opinion such levy could have been made.

It is difficult to understand why any distinction should be made between this case and one where crops are growing on a statutory homestead, which is exempt under the Bankrupt Act. In such instance no creditor could claim that the land passed to the trustee; no creditor would have the right to the labor of the bankrupt in maturing, harvesting and marketing the crop. Yet the authorities are uniform in holding that in such cases the title to the crop would pass to the trustee.

It is equally difficult to conceive how the court could conclude that this crop was not subject to levy and sale,

> "because otherwise the owner thereof might be prevented from performing the conditions precedent, of which was cultivation of the crop, with the government".

How could a levy or sale of the growing crop possibly prevent or interfere with a bankrupt's performance of the necessary conditions precedent to his right to the homestead? He would still retain the possession of the land. It would still be producing and bearing crops. All the requisites of the United States Homestead Act would be complied with. The only possible difference would be that the entryman would be deprived of his crop, but we know of no statute which this would violate and

cannot understand how it could possibly endanger his homestead right. That the bankrupt could abandon his homestead rights, plow up the crop, or otherwise destroy it, is immaterial, because such acts *would only go to the value of the right* sought to be gained by the levy, and not *the right itself*.

The rights of the bankrupt in growing crops has been before the federal courts many times, as shown by the following authorities:

In re Sullivan, 148 Fed. 115;
In re Daubner, 76 Fed. 805;
In re Frederick, 28 Am. Bnk. Reg. 656;
In re Hoag, 97 Fed. 503.

In re Tiffany, 93 Fed. 427.

In each instance the federal court has held that the growing crop passes to the trustee in bankruptcy.

In re Sullivan, supra, the court held that crops of ripe grain growing on a homestead are not exempt unless made so by the State statutes or decisions. The bankrupt in that case claimed the crop was exempt because it was the product of exempt property, namely, his homestead. The court said:

> "If all growing crops upon an exempt homestead are *ipso facto* exempt anyone may secure a homestead near a large city, expend much money in seed, in fertilizing the ground and in growing and harvesting the crops, and in that way secure large returns from vegetable and other products, sell them in a convenient and available market, accumulate a fortune and successfully defy creditors. Such possibility demonstrates that the theory of law which makes it possible is probably not sound, and in-

> duces fraud from a construction of the statute, if the same could be reasonably done, which will not permit it."

In re Hoag, supra, the court holds that where the State statute exempts a homestead the bankrupt cannot claim as exempt, in addition thereto, the crops growing on the land at the time of filing his petition in bankruptcy. The court said:

> "Growing crops are personal property in law. Although on a sale of the land without reservation, they go with the land because the implication is clear that such is the intention, they pass by bill of sale or chattel mortgage without sale, and even by oral agreement, and may be levied upon by execution or attachment as personal estate, and on the death of the owner descend to his personal representatives, and not to his heirs. It is also claimed that the crops are exempt as being the product of a homestead which is itself exempt. If this be so it would follow that cattle, horses, and other stock grown on the homestead are also exempt for the same reason. So that it would be possible for a thrifty debtor with an eye to business to easily double or quadruple the exemptions enumerated by the statute."

In re Daubner, supra. This case holds that land acquired under homestead law of the United States cannot be subject to bankruptcy proceedings for the payment of any debt contracted before the issuance of patent, yet crops growing on such homestead at the time of the adjudication of a voluntary bankrupt, are not exempt but pass to the trustee for the benefit of creditors. The court said:

> "While for many purposes growing crops are held to be a party of the realty yet in many

cases they have been treated as personalty and held liable to attachment or execution and levy and sale. Upon a sale of the land the growing crops, unless reserved, would pass to the purchaser, but they are capable of reservation and of mortgage and sale to the owner of the land, and when such owner voluntarily goes into bankruptcy he must be held to the intent that such of his property and rights as are the subject of disposition by him, and are not necessarily exempt, shall vest in the trustee for the benefit of creditors. Such crops are the fruits of the bankrupt's industry or of his investment of money, or both. It would be productive of great injustice if the owner of a homestead is permitted to spend his money upon exempt land, and then between such time and harvest procure a discharge in bankruptcy, and so reap what was sown at the expense of the creditor. By such device the bankrupt might secure a discharge from his debts and retain his property, with its increase, and the bankruptcy law be made a mistreatment of law."

We therefore submit that the order of the order of the District Court of the United States for the District of Montana reversing the order of the Referee, be itself reversed, and the order of the Referee reinstated.

Dated, San Francisco,
October 15, 1915.

Respectfully submitted,

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Attorney for Petitioner.